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IN THE

Supreme Court of the United States

October Term, 1941.

No. 838

GEORGE T. GOGGIN, as Trustee in Bankruptcy of the Estate of Acme Traffic Signal Company, a corporation,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

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IN THE

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No. .....

GEORGE T. GOGGIN, as Trustee in Bankruptcy of the Estate of Acme Traffic Signal Company, a corporation,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable Harlan P. Stone, Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

May it please the Court:

The petition of George T. Goggin respectfully shows to this Honorable Court:

I.

Summary Statement of Facts.

The facts in this case are:

Acme Traffic Signal Company was a California corporation. Originally it instituted and prosecuted proceedings in the United States District Court for the Southern District of California for reorganization under Chapter X

of the Bankruptcy Act. Failing in reorganization, the corporation was adjudged a bankrupt in the same proceeding on May 13, 1940, and the case referred to a Referee in Bankruptcy for administration. Upon the Trustee's refusal to sign a return prepared by the Collector of Internal Revenue for the capital stock tax for the fiscal year ending June 30, 1940, the Collector, under authority of Section 3612 of the Internal Revenue Code, made the return. In it the Collector started with the adjusted declared value of $198,412.46, reported in the company's 1939 capital stock tax return made by the officers of the bankrupt corporation prior to the filing by the company of its proceeding under Chapter X. From this amount $13,446.20 was deducted as the amount of loss occurring during the previous income tax year according to the taxpayer's books. Thus an adjusted declared value of $184,-966.26 was arrived at for the fiscal year ending June 30, 1940. A capital stock tax of $184.00 was computed and assessed for such fiscal year ending June 30, 1940. But, since Section 204 of the Revenue Act of 1940, enacted after the preparation and filing of the Federal Government's capital stock tax claim in the bankruptcy proceeding, provided for an increase in the amount of the tax by 10%, the total tax for which claim was finally made was $202.00. It is conceded that the capital stock of the bankrupt had an actual fair market value at less than $184,000 on June 30, 1940, and that the Trustee in Bankruptcy was able to obtain only $5100 from the sale of all of the bankrupt's assets.

The Referee in Bankruptcy, over the objections of the Trustee in Bankruptcy, allowed the tax claim. Upon review the order of the Referee was reversed by the Judge of the District Court. Upon appeal by the Federal Government from this judgment of the District Court the Circuit Court of Appeals for the Ninth Circuit, by its judgment made November 18, 1941, reversed it. No petition for rehearing has been filed or is pending in the Circuit Court of Appeals. The claim thus stands allowed at $202.00.

The Referee did not state his reasons for his decision. The opinion of the District Court is reported in 37 Fed. Supp. 352, 45 A. B. R. (N. S.) 346, and is a part of the record before the Supreme Court [Tr. p. 2]. The opinion of the Circuit Court of Appeals is likewise of record [Tr. p. 40].

The theory of the District Judge was that the Bankruptcy Court had full power, under Sections 62-a and 64-a of the National Bankruptcy Act of 1898, as amended by the Chandler Act, to hear and determine whether the value which formed the basis of the assessment for the computed capital stock tax was a proper and correct value, as provided by Section 1200-(a) *et seq.* of the Internal Revenue Code.

Section 62-a of the Bankruptcy Act provides:

> "Sec. 62a. The actual and necessary costs and expenses incurred by officers in the administration of estates shall, except where other provisions are made for their payment, be reported in detail, under oath,

and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred."

Since the period for which the Federal Government claims the taxes due is partly before the bankruptcy, viz., up to May 13, 1940, and partly afterwards, viz., May 13 to June 30, 1940, Section 62-a may have some application here. Taxes accruing after the commencement of bankruptcy proceedings are expenses of administration of the bankrupt estate on a parity with other expenses.

Missouri v. Earhart, 111 Fed. (2d) 992, 42 A. B. R. (N. S.) 634;

In re Cal. Pea Products (D. C. S. D. Cal.), 37 Fed. Supp. 658, 45 A. B. R. (N. S.) 393;

In re Lambertville Rubber Co. (C. C. A. 3), 111 Fed. (2d) 45, 42 A. B. R. (N. S.) 697;

In re Columbia Ribbon Co. (C. C. A. 3), 117 Fed. (2d) 999, 45 A. B. R. (N. S.) 528.

Section 64-a-(4) of the Bankruptcy Act provides:

". . . in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court (court of bankruptcy);"

As stated by the District Judge in his opinion:

"Whether the determination of the question under consideration is under Section 64-a-(4) or under Section 62 of the Bankruptcy Act, as an expense of

administration, the power of the Bankruptcy Court to decide the matter is co-extensive in either situation."

The theory of the Circuit Court of Appeals, in its opinion, is that the plain import of the Revenue Act and the Treasury Regulations is that the capital stock tax for the fiscal year ending June 30, 1940, was a tax levied as against the corporation for the privilege of carrying on and doing business for the whole or any part of such fiscal year and that, since the corporation did carry on and did do business throughout that fiscal year and up until the adjudication of bankruptcy May 13, 1940, such capital stock tax had, in fact, accrued and the bankruptcy could not work any change in the method of its ascertainment or of the amount of the tax. And, further, that the tax was an indebtedness of the corporation the same as any obligation owed by it at the time of the bankruptcy proceedings and must be so treated.

II.

Issue Involved.

The issue involved in this case is as follows:

Should the capital stock tax due from the bankrupt corporation for the taxable fiscal year ending June 30, 1940, be determined on the basis of the adjusted declared value of the capital stock as determined by the Collector of Internal Revenue under the applicable revenue act, or on the basis of the actual value of the assets of the bankrupt corporation during the period involved.

III.

Reasons Relied on for the Allowance of the Writ.

1. **Necessity of a Clarification of the Application of the Recent Decision of the United States Supreme Court in the Case of Arkansas Corporation Commission v. Thompson.**

An uncertainty now exists in Bankruptcy Courts, owing to the language of the Court in the opinion in the recent decision of the United States Supreme Court in the case of *Arkansas Corporation Commission v. Thompson*, decided April 28, 1941, 85 L. Ed. Adv. Op. 801, as to (a) the power of Bankruptcy Courts to determine, under Section 64-a-2 of the Bankruptcy Act, as amended by the Chandler Act, the legality and amount of tax claims filed against bankrupt estates and accruing prior to the commencement of the bankruptcy proceeding, and (b) the power of the Bankruptcy Court to determine, under Section 62-a of the Bankruptcy Act, as amended by the Chandler Act, the legality and amount of tax claims presented against bankrupt estates as expenses of administration. A serious question has arisen as to whether the Bankruptcy Court can go behind the determination of a taxing agency as to the amount of the tax and itself fix the proper amount after reviewing the facts. The tax involved in that case was one arising after the commencement of the bankruptcy, *i. e.*, an expense of administration and, therefore, subject to Section 62-a and not Section 64-a-(4). The bankruptcy was a railroad reorganization under Section 77. The Court expressly declined to decide whether Section 64-a-(4) applied to proceedings under Section 77. The decision of the Court, so far as it is confined to the facts of the case, appears to be based upon sound principles, since the trustee, with the consent of

the Bankruptcy Court, submitted himself to the jurisdiction of the Arkansas Corporation Commission for the determination of the tax after a hearing. He was bound by its decision upon the doctrine of *res judicata.*

But the difficulty is that the Court, in the latter part of its opinion, probably by way of *obiter dicta*, uses language indicating that the Bankruptcy Court does not have power to determine the amount of the tax where the same has been fixed by a taxing agency, even though the basis of the tax is false or the tax itself is based upon an excessive assessment. The Court states:

> "But there is nothing in the history of bankruptcy or reorganization legislation to support the theory that Congress intended to set the federal courts up as super-assessment tribunals over state taxing agencies. The express legislative purpose of Arkansas to move towards a more nearly uniform and fairly distributed tax burden through relying on supervision by a single agency could be in large part frustrated by the construction of the Bankruptcy Act for which the trustee here contends. Section 64-a, thus construed, would tend to obstruct, and not to facilitate, the enforcement of the state tax laws. Nothing in the language of the Act requires such a construction. And the policy of revising and redetermining state tax valuations contended for by the trustee would be a complete reversal of our historic national policy of federal non-interference with the taxing power of the states."

As a result of the decision tax assessors all over the country are contending that they are quasi-judicial agencies because, in fixing assessments, they have the power to gather evidence and hold hearings and, therefore, their determinations, even though the bankrupt or the trustee take no part therein, are binding upon the Bankruptcy Court.

Judge Harry A. Hollzer of the United States District Court for the Southern District of California, Central Division, in the unreported case of *In re Santa Fe Distilleries,* No. 32,667-H in Bankruptcy, has held that, in view of such decision, the Bankruptcy Court does not have power to review and revise tax assessments, at least with respect to those made by state taxing agencies.

It would seem that the determination of a tax by a taxing agency would not have any greater force than a judgment of a court of competent jurisdiction. In the case of *Pepper v. Litton,* 308 U. S. 295, 84 L. Ed. 281, 41 A. B. R. (N. S.) 279, the Supreme Court held that the Bankruptcy Court, at least where *res judicata* is not involved, could go behind the underlying debt to ascertain whether the judgment was just or not.

The real theory of the Arkansas case, as we see it, is that the trustee, by undertaking to challenge the assessment before the Corporation Commission and by failing to appeal therefrom as provided by law, was estopped to challenge the result in the Bankruptcy Court.

Collier on Bankruptcy, 14th Ed., Vol. 3, p. 2166, Note. 60.

2. Conflict of the Decision of the Ninth Circuit With the Decisions of Other Circuit Courts of Appeals.

If we assume that the decision of the Supreme Court in the *Arkansas Corporation Commission v. Thompson* case does not go so far as to deprive the Bankruptcy Courts of the power to determine the proper amounts of tax claims, whether fixed by state or federal taxing agencies, at least in the absence of a plea of *res judicata,* then we run into a conflict between the decisions of the Ninth Circuit in this case and the decisions of other Circuit Courts of Appeals wherein it is held that the Bankruptcy Courts have full power to revise the amount of any such tax claims.

See:

Henderson County v. Wilkins (C. C. A. 4), 43 Fed. (2d) 610, 16 A. B. R. (N. S.) 359;

Dickinson v. Riley (C. C. A. 8), 32 A. B. R. (N. S.) 279;

City of Springfield v. Hotel Charles Co. (C. C. A. 1), 31 A. B. R. (N. S.) 604, 84 Fed. (2d) 589.

It appears that the Seventh Circuit, in the case of *In re 168 Adams Building Corp.,* 40 A. B. R. (N. S.) 754, 105 Fed. (2d) 704, supports the decision of the Ninth Circuit in our particular case. The Ninth Circuit itself, in the previous case of *In re Florence Commercial Co.,* 19 Fed. (2d) 468, 10 A. B. R. 284, indicated, while not directly deciding, that in its opinion the Bankruptcy Court did have jurisdiction to review the amount of tax claims.

3. The Circuit Court of Appeals for the Ninth Circuit Has Decided an Important Question of Federal Bankruptcy Law Which Has Not Been, but Should be, Finally Settled by the Supreme Court of the United States.

That this is the situation is exemplified by the comments of Professor James Wm. Moore, editor-in-chief of the new *Collier on Bankruptcy*, 14th edition, volume 3, pages 2143 *et seq.*, wherein he discusses the case of *Arkansas Corporation Commission v. Thompson*, decided April 28, 1941, 85 L. Ed. Adv. Op. 801. The facts in that case were: The Arkansas Corporation Commission is a state agency, vested with authority in the regulation of certain public utilities, including railroads. Also, in the administration of the state tax laws, the Commission has supervision over the valuation, assessment and equalization of all property. It has power to summon witnesses and hear evidence. Before assessments are finally determined all persons interested have the right, on written application, to appear and be heard. In 1939 the Missouri Pacific Railroad was being operated in Arkansas by a trustee in Section 77 proceedings under the Bankruptcy Act. The Commission, after a hearing in which the trustee participated, fixed the value of the railroad's Arkansas property and levied an assessment for 1939. The trustee's motion for rehearing was heard, considered and overruled by the Commission. The trustee did not appeal to the state courts, as he had a right to do, from these decisions of the Commission. The trustee then sought to have the Bankruptcy Court fix the validity and amount of this assessment. While the lower federal courts held that this could be done, the Supreme Court held it could

not. Professor Moore states: Until the decision of the United States Supreme Court in *Arkansas Corporation Commission v. Thompson* the great weight of authority was that the Bankruptcy Court had full power to examine into the validity and *amount* of taxes constituting the basis for prior claims in bankruptcy and to ascertain from the evidence presented the legality of the tax and the amount of the valuation which should be used as the basis for the assessment. He further states that it was a generally-accepted view that even a determination, after hearing, by a duly constituted state tax board agency was not conclusive as to the Bankruptcy Court, although it was held that, with respect to federal taxes, a determination by the Board of Tax Appeals could not be controverted. Also that it was the preponderate weight of authority that an assessment by and under the authority of a tax collector or assessor, a Collector of Internal Revenue, or the Commissioner of Internal Revenue, was subject to redetermination by the Bankruptcy Court. Professor Moore further states that it now appears settled, in view of the Arkansas case, that where a duly constituted *quasi*-judicial agency, state or federal, has passed upon a tax claim by due hearing thereon, the Bankruptcy Court cannot redetermine such claim or alter its amount unless (a) the agency has made an improper arithmetical computation, or (b) has acted beyond its legal powers, or (c) the assessment has been tainted by discernible illegality under the applicable tax law as distinguished from a mere alleged over-assessment based on an assessed value. Further than this he states light is needed. There is not in

the Arkansas case any solution of the problem as to whether or not the trustee is concluded by the acts or omissions of the bankrupt where a *quasi*-judicial agency has not passed upon the tax claim. Under the view contended for in the cases of *In re Gould Mfg. Co.* (D. C. Wis.), 29 A. B. R. (N. S.) 733, 11 Fed. Supp. 644; *In re 168 Adams Building Corp.* (D. C. Ill.), 40 A. B. A. (N. S.) 444, 27 Fed. Supp. 247, affirmed (C. C. A. 7) 40 A. B. R. (N. S.) 754, 105 Fed. (2d) 704, and companion cases, that an assessment by a tax assessor or similarly empowered officer would be in the same category as that made by a *quasi*-judicial taxing agency, it might be argued that, inferentially, the Arkansas case supports this view, since those cases are cited therein with apparent approval. On the other hand, credence is given to the opposite conclusion in that the court, in distinguishing the previous Supreme Court case of *State of New Jersey v. Anderson*, 203 U. S. 483, 17 A. B. R. 63, 51 L. Ed. 284, stressed the fact that the state board there acted in an administerial capacity rather than a *quasi*-judicial one. Professor Moore concludes his dissertation on the subject at page 2167, where he states that until the point has been squarely decided by the Supreme Court he feels that the weight of authority still prevails that the bankruptcy estate may obtain a revaluation where the assessment is clearly shown to be grossly excessive and the assessment has not progressed beyond the stage where a tax assessor or some similar officer, not acting in a *quasi*-judicial capacity, has made the determination.

4. The Effect of the Decision of the Ninth Circuit Is to so Cloud the Question of the Power of the Bankruptcy Court, Under Both Section 64-2-(4) and Section 62-a of the Bankruptcy Act, to Determine the Amount and Legality of Tax Claims, Particularly Where They Are Upon a False Basis or Are Based Upon an Excessive Assessment, That an Authoritative Decision of the Supreme Court Is Required to Clarify the Law, Not Only for the Benefit of Taxpayers Throughout the Nation but Also for the Benefit of State and Federal Governments Themselves.

With mounting taxation all over the country, state and federal, bankrupt estates are easy prey for the ready collection of tax money. Sometimes bankrupt estates have to contend with about a dozen different kinds of taxes. The smaller estates are usually so overwhelmed with taxes as prior debts that they are entirely swallowed up before there is even a nibble left for the general creditors.

The time has arrived, in the interest alike of debtors, bankrupts, creditors, trustees in bankruptcy and taxing agencies, both state and federal, for a clarification, as far as is possible, in view of the existing laws and cases, of the power of Bankruptcy Courts to determine the legality and, particularly, the *amount* of tax claims with respect to the following situations:

(a) Where the debtor or bankrupt, prior to bankruptcy, fails to avail himself of the methods provided by state or federal laws for the review of tax assessments which are false or excessive.

(b) Where the debtor or bankrupt, prior to bankruptcy, avails himself of such methods to the extent that

the final determination by the state or federal taxing authority, whether *quasi*-judicial or not, is *res judicata* as to him, but not as to creditors or his subsequent trustee in bankruptcy.

(c) Where the trustee in bankruptcy fails to avail himself of the methods provided by state or federal laws for the review of false and excessive assessments made before bankruptcy for taxes accruing prior to that time, and awaits the filing of the tax claim against the bankrupt estate and then invokes Section 64-a-(4), which appears to give the Bankruptcy Court the power to determine the legality and amount of such taxes.

(d) Where the trustee in bankruptcy, with respect to taxes accruing after bankruptcy, as expenses of administration, fails to avail himself of such methods, and awaits the presentation of the tax claim to the Court for payment and then invokes Section 62-a, which gives the Bankruptcy Court the power to fix and determine expenses of administration.

The instant case furnishes an excellent vehicle for this purpose.

IV.

Brief in Support of This Petition.

Attached to this petition, and as a part of the same, is a brief in support thereof.

Wherefore, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the said Circuit Court of Appeals for the Ninth Circuit commanding that Court to certify and send to this Honorable Court for its review and determination, on a day to be named therein, a full and complete transcript of the record and all proceedings in the case numbered 9805 in that Court and entitled "United States of America, Appellant, vs. George T. Goggin, as Trustee in Bankruptcy of the Estate of Acme Traffic Signal Company, a corporation, bankrupt, Appellee," and that its judgment therein made on November 18, 1941, may be reversed by this Honorable Court; and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

Dated at Los Angeles, California, this 18th day of December, 1941.

GEORGE T. GOGGIN,
Trustee in Bankruptcy of the Estate of Acme Traffic Signal Company, a Corporation, Petitioner,

By REUBEN G. HUNT,
His Counsel.

ROBERT B. POWELL,
GRAINGER & HUNT,
Of Counsel for Petitioner.

Certificate of Counsel.

I hereby certify that I am counsel for the petitioner in the above-entitled cause and that, in my judgment, the foregoing petition is well founded in law and fact, and that the said petition is not interposed for delay.

Dated this 18th day of December, 1941.

REUBEN G. HUNT,
Counsel for Petitioner.

IN THE

Supreme Court of the United States

October Term, 1941.

No. .....

GEORGE T. GOGGIN, as Trustee in Bankruptcy of the Estate of Acme Traffic Signal Company, a corporation,
Petitioner,

vs.

UNITED STATES OF AMERICA,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

The opinion of the District Court appears at page 2 of the record. See, also, 37 Fed. Supp. 352, 45 A. B. R. (N. S.) 346.

The opinion of the Ninth Circuit Court of Appeals appears at page 40 of the record. See, also, C. C. H. Bankruptcy Service, page 53,768, paragraph 53,479.

The Referee did not file an opinion.

II.

Jurisdiction.

Jurisdiction herein is predicated upon Judicial Code, Section 240-a, as amended by the Act of February 13, 1935, Chap. 229, Section 1, 43 Stat. 936.

Reference is made, also, to Rule No. 38-5-(b) of the Supreme Court, wherein is specified some of the reasons

which will be considered by the Supreme Court in the exercise of its sound judicial discretion with respect to the issuance of writs of certiorari.

III.

Statement of the Case.

This has been covered under headings Nos. I and II in the foregoing petition for the writ of certiorari. For the sake of brevity the statement is not repeated here.

IV.

Specification of Errors.

The following are assigned as errors in connection with the judgment of the Ninth Circuit Court of Appeals made on November 18, 1941:

(1) Its holding that the determination of an adjusted capital stock tax by the Collector of Internal Revenue. based upon a concededly false value, cannot be reviewed and revised by the Bankruptcy Court, either under Section 64-a-(4) or Section 62-a of the Bankruptcy Act.

(2) Its holding that such a tax, so ascertained, is the same as any other obligation owed by the debtor or bankrupt at the time of the commencement of the bankruptcy proceedings; and that the debt itself cannot be reviewed and revised under the general equity powers of the Bankruptcy Court and its control over claims filed against the bankrupt estate, to ascertain whether such tax is a just debt against the estate.

(3) Its holding, in effect, that the declared capital stock value by the bankrupt, prior to bankruptcy, even though false, is irrevocable and binding upon the Bankruptcy Court.

V.

ARGUMENT.

POINT 1.

Bankruptcy Courts Have Ample Power to Review and Revise Tax Claims, Whether They Arise Before Bankruptcy or Afterward.

Tax claims arising before bankruptcy are properly claims against the estate and subject to Section 64-a-(4). Bankruptcy Act, Sec. 57-n; *City of New York v. Feiring,* 45 A. B. R. (N. S.) 643, 85 L. Ed. Adv. Op. 892. Tax claims arising after bankruptcy are properly expenses of administration and subject to Section 62-a.

Missouri v. Earhart (C. C. A. 8), 111 Fed. (2d) 992;

In re Cal. Pea Products (D. C. S. D. Cal.), 37 Fed. Supp. 658, 45 A. B. R. (N. S.) 393;

In re Lambertville Rubber Co. (C. C. A. 3), 42 A. B. R. (N. S.) 697, 111 Fed. (2d) 45; and

Columbia Ribbon Co. (C. C. A. 3), 117 Fed. (2d) 999, 45 A. B. R. (N. S.) 528.

The Bankruptcy Act appears to give the Bankruptcy Court ample control over such claims. Section 2-a-(2) provides that the Bankruptcy Court has jurisdiction to

> "Allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates."

Section 64-a-(4), relating to debts which have priority, provides:

> "That, in case any question arises as to the amount of legality of any taxes, such question shall be heard and determined by the court."

Section 62-a, relating to expenses of administering estates, provides:

> "The actual and necessary costs and expenses incurred by officers in the administration of estates shall . . . be . . . examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred."

Also, it would seem that a tax claim, state or federal, would have no higher standing as a claim than a judgment by a court of competent jurisdiction. In the exercise of its general equity powers the Bankruptcy Court, at least in the absence of a plea of *res judicata*, can go behind a judgment claim to ascertain whether the underlying debt is just and equitable.

> *Pepper v. Litton*, 308 U. S. 295, 85 L. Ed. 281, 41 A. B. R. (N. S.) 279.

POINT 2.

The Fact That the Federal Statute Makes Irrevocable a Declaration of Capital Stock Value by a Taxpayer Does Not Preclude the Bankruptcy Court From Adjusting the Tax From the Point of View of Whether or Not Such Declared Value Is the True Value.

In the instant case it was the contention of the federal government, upheld by the Circuit Court of Appeals, that, since the statute (Sec. 1202-a-(2) of the Internal Revenue Code) does not permit any amendment by the taxpayer of a capital stock value once declared by him, or, in other words, such declaration is irrevocable, the Bankruptcy Court is helpless to go behind this declared value, ascertain the actual value, and allow or disallow the tax claim accordingly.

In our case, in the District Court, Judge McCormick said:

> "The purpose of establishing an irrevocable adjusted declaration of value by a corporate taxpayer as the basis of its capital stock tax is to protect the government from avoidance by the taxpayer of just capital stock taxes and the interrelated excess profits tax, as well. See *Chicago Telephone Supply Co. v. United States* (Court of Claims), 23 Fed. Supp. 471."

As further stated by Judge McCormick in his opinion:

> "It is impossible for this bankrupt to avoid any taxes which it is reasonably obligated to pay under the undisputable facts shown by the record before us; therefore the reason for the rule of binding declared value is absent and the rule is inapplicable to this proceeding."

The taxable entity, the bankrupt, is not relieved of its obligation to pay the tax. The debt is not dischargeable.

Bankruptcy Act, Section 17-a. The new entity, the Trustee representing creditors, who were not parties to the transactions between the federal government and the bankrupt, and who are entirely innocent, should not be required to relieve the bankrupt of this burden.

But this view of the appellate court overlooks the principle that the taxpaying entity changes when bankruptcy commences. The Trustee in Bankruptcy, while successor to the title to the property of the bankrupt by operation of law, primarily represents the unsecured creditors. *In re American Fidelity Corp.* (D. C. S. D. Cal.), 28 Fed. Supp. 462, 40 A. B. R. (N. S.) 379. This subject is tersely summarized in the opinion of Judge McCormick in the District Court in the instant case.

> "Here we find a bankrupt corporation at no time subsequent to May 13, 1940, 'carrying on or doing business,' but where all of the activities of its trustee are directed to the liquidation and distribution in accordance with the ordinary processes of the Bankruptcy Act. In such a case, under the express authority of Section 64-(a) of the Bankruptcy Act an obviously arbitrary and fictitious value as the basis of a tax against the trustee is not conclusive against him. By reason of the broad investiture of power under the Bankruptcy Act the Bankruptcy Court cannot be precluded from ascertaining and determining the amount of the capital stock tax, if any, that is assessable and chargeable against the bankrupt estate because some entity, unauthorized by the court, has at some earlier time made a commitment with respect to the capital value of the corporation when the company was carrying on and doing business. New Jersey v. Anderson, 203 U. S. 483, 17 Am. B. R. 63."

POINT 3.

Any Estoppel That Might Attach to the Bankrupt Would Not Necessarily Attach to the Trustee or the Creditors, Since They Were Not Parties to the Transaction Out of Which the Estoppel Arose.

The bankrupt corporation formally declared a capital stock value. The Commissioner adjusted this to a lower figure. If the bankrupt is estopped to question the figure arrived at, is the Trustee, representing creditors also estopped? We think not. The Trustee and the creditors were not parties to the transaction out of which the estoppel might arise. They had no part in the declaration of value. Estoppel affects only the immediate parties to the transaction and their privies. *Roper v. Smith*, 45 Cal. App. 302. With respect to the Trustee's right to contest claims for taxes levied against a bankrupt's property, the doctrine of estoppel is inapplicable since there is no privity between the Trustee and the bankrupt. The Trustee acquired title to the property of the bankrupt by operation of law only. *In re Gustav Schaeffer Co.* (C. C. A. 6), 103 Fed. (2d) 237, 39 A. B. R. (N. S.) 617. The Trustee represents the general creditors and in this capacity may assert claims, defend against them, avoid preferences, and collect assets where the bankrupt, if bankruptcy had not intervened, would be estopped. *In re Kessler* (C. C. A. 2), 186 Fed. 127, affirmed, *Merchants' Natl. Bk. v. Secton*, 228 U. S. 634, 57 L. Ed. 998, 30 A. B. R. 278.

POINT 4.

The Doctrine of Res Judicata Has No Application Here, Either as to the Bankrupt or the Trustee.

This appears to be obvious, since neither the bankrupt nor the Trustee participated in any hearing before any federal judicial, or *quasi*-judicial agency. The case of *Arkansas v. Thompson, supra*, would seem not to apply. Even though the bankrupt were bound by *res judicata*, this would not restrict the Trustee nor the creditors. *Res judicata* affects only the parties themselves to the suit or proceeding.

Edmonds v. Glenn-Colusa Irrigation District, 217 Cal. 436.

POINT 5.

Once Bankruptcy Intervened the General Creditors, Represented by the Trustee, Had the Right to a Determination by the Bankruptcy Court as to Whether or Not the Previously Declared Capital Stock Value or the Subsequently Adjusted Value Was Excessive, Irrespective of Whatever Action May or Could Have Been Taken by the Bankrupt Under Applicable State or Federal Law, Short of an Actual Prior Determination by Another Court That Would Be Binding Upon the Trustee.

The cases supporting this doctrine are numerous and are collected in *Collier on Bankruptcy*, 14th Ed., Vol. 3, 2149, Note 25:

In re Seaver-Howland Press, Ref., Mass., 16 A. B. R. (N. S.) 227;

Comacho v. Int. Express & Foundry Co. (D. C. Porto Rico), 48 A. B. R. 317;

In re Gustav Schaefer Co. (C. C. A. 6), 103 Fed. (2d) 237, 39 A. B. R. (N. S.) 617;

In re E. C. Fisher Corp. (D. C. Mass.), 229 Fed. 316, 36 A. B. R. 509;

In re Raflowitz (D. C. Conn.), 37 Fed. Supp. 202, 45 A. B. R. (N. S.) 11;

In re R. Suarez & Co. (D. C. Porto Rico), 48 A. B. R. 316;

In re Otto Freund Arnold Yeast Co. (D. C. N. Y.), 178 Fed. 305, 24 A. B. R. 458;

County of Henderson v. Wilkins (C. C. A. 4), 43 Fed. (2d) 670, 16 A. B. R. (N. S.) 359;

In re Willett-Baker Lumber Co. (D. C. E. D. N. Y.), 31 Fed. Supp. 130, 41 A. B. R. (N. S.) 339.

POINT 6.

A Prime Purpose of the Bankruptcy Act Is to Provide Machinery Whereby Bankrupt Estates Can Be Administered Economically and Closed Promptly.

Unless the Bankruptcy Court can invoke the powers apparently granted them for this purpose by Sections 2-a-(4), 64-a-(4) and 62-a of the Bankruptcy Act, this objective cannot be attained. Under the broad powers granted by these sections, as we construe them, the delays incident to the ordinary procedure governing the collection of taxes are thus avoided and the early settlement of the bankrupt's estate is greatly facilitated.

Cohen v. United States (C. C. A. 1), 115 Fed. (2d) 505, 44 A. B. R. (N. S.) 489;

In re Sheinman (D. C. E. D. Pa.), 14 Fed. (2d) 323, 8 A. B. R. (N. S.) 623;

In re Universal Rubber Products Co., 25 Fed. (2d) 168, 11 A. B. R. (N. S.) 183, affirmed (C. C. A. 3), 28 Fed. (2d) 253, 12 A. B. R. (N. S.) 698;

In re W. P. Williams Oil Corp. (D. C. W. D. Ky.), 265 Fed. 401, 45 A. B. R. 278;

In re Clayton Magazines (C. C. A. 2), 77 Fed. (2d) 852, 29 A. B. R. (N. S.) 97.

POINT 7.

A Determination After Hearing by a Duly-Constituted Tax Board or Agency, Where the Trustee or the Creditors as a Whole Were Not Parties, Is Not Conclusive on the Bankruptcy Court.

The cases on this subject are collected in *Collier on Bankruptcy*, 14th Ed., Vol. 3, p. 2147, Notes 13 and 14:

In re Denver & Rio Grande R. Co. (D. C. Col.), 23 Fed. Supp. 298, 37 A. B. R. (N. S.) 156;

In re Seaver-Howland Press (Ref. Mass.), 16 A. B. R. (N. S.) 227;

In re Becker (Ref. N. J.), 12 A. B. R. (N. S.) 732;

Dickinson v. Reilly (C. C. A. 8), 86 Fed. (2d) 385, 32 A. B. R. (N. S.) 279;

In re Thermiodyne Radio Corp. (D. C. Del.), 26 Fed. (2d) 716, 12 A. B. R. (N. S.) 192;

State of New Jersey v. Anderson, 203 U. S. 483, 51 L. Ed. 284, 17 A. B. R. 63;

Contra: Kelly v. United States (C. C. A. 9), 90 Fed. (2d) 73, 34 A. B. R. (N. S.) 191.

POINT 8.

The Supreme Court Has Held That a Sale Free of the Lien of a Tax Claim May Be Held in Bankruptcy and the Taxing Agency Remitted to the Proceeds of the Sale for the Collection of the Taxes.

So held in the case of *Van Huffel v. Harkleroad*, decided Dec. 7, 1931, 284 U. S. 225, 76 L. Ed. 256, 18 A. B. R. (N. S.) 730. There the Court stated:

> "No good reason is suggested why liens for state taxes should be deemed to have been excluded from the scope of this general power to sell free from encumbrances. Section 64 of the Bankruptcy Act grants to the court express authority to determine 'the amount or legality' of any tax. To transfer the lien from the property to the proceeds of its sale is the exercise of a lesser power; and legislation conferring it is obviously constitutional. Realization upon the lien created by the state law must yield to the requirements of bankruptcy administration."

We see no conflict between this case and the *Arkansas* case. The earlier case distinctly states that the ***amount*** as well as the *legality* of taxes may be determined by the Bankruptcy Court. The earlier case is not overruled or distinguished in the *Arkansas* case. It is not even referred to.

POINT 9.

The Declared Value of Capital Stock May Not Be Arbitrary and Fictitious, but Should Have a Fair Relationship With the Actual Value.

The federal government may contend that the capital stock on which the tax is imposed bears no relationship to the actual value of such stock and was not intended to bear any such relationship. In other words, each individual taxpayer has a right to arbitrarily declare the value regardless of actual value; and can make the best guess possible as to the future of his business and then based upon that guess to arbitrarily declare a value for the stock which would place his combined capital stock tax and excess profits tax at a minimum, which valuation would in many cases bear no relationship to the actual value. This contention is exploded in the case of *Kentucky Fire Brick Co. v. Glenn*, D. C., W. D., Ky., 34 Fed. Supp. 35. In that case it was held that the taxpayer should make the declaration of value consistent with the facts, with reasonable latitude allowed for difference in judgment, and should exercise good faith in the declaration, since "value" has a definite meaning which is radically different from selecting a figure at will. It was further held that the purpose of the statute imposing capital stock taxes upon corporations was to impose a tax based on fair and reasonable value rather than upon arbitrary value. Also that the restriction that the value first declared could not be changed, did not apply and was not conclusive if the taxpayer acted arbitrarily or fraudulently in declaring such value with the result that the tax was based upon a false and fictitious value.

VI.
Conclusion.

We contend that false or excessive taxes should not be allowed against bankrupt estates, unless the Bankruptcy Act is so framed that the Bankruptcy Court is powerless to overcome the evil. We maintain that our exposition of the subject above, shows that it is not. The Bankruptcy Court, in its exclusive control over the administration of the estate, can either decide these matters itself, or remit the trustee to a state court or *quasi*-judicial agency, or another federal court, or *quasi*-judicial agency, of competent jurisdiction, to make the determination. *In re Baldwin,* 291 U. S. 610, 78 L. Ed. 20, 24 A. B. R. (N. S.) 487; *Thompson v. Magnolia Petroleum Co.,* 309 U. S. 478, 84 L. Ed. 876, 42 A. B. R. (N. S.) 216; *In re American Fidelity Corp.* (D. C. S. D. Cal.), 28 Fed. Supp. 462, 40 A. B. R. (N. S.) 379. We do not see anything in the *Arkansas* case to the contrary. Nor should any state government, or the federal government insist upon the collection of false and excessive taxes. Governments expect their citizens to deal fairly with them in the payment of taxes. Governments should likewise deal fairly with its citizens in the assessment and collection of taxes, especially where this is sought from the beneficiaries of bankrupt estates, the creditors, who are innocent parties and have not had any participation in the transactions between the debtors and the taxing agencies.

United States v. Middle States Oil Co. (C. C. A. 8), 18 Fed. (2d) 231.

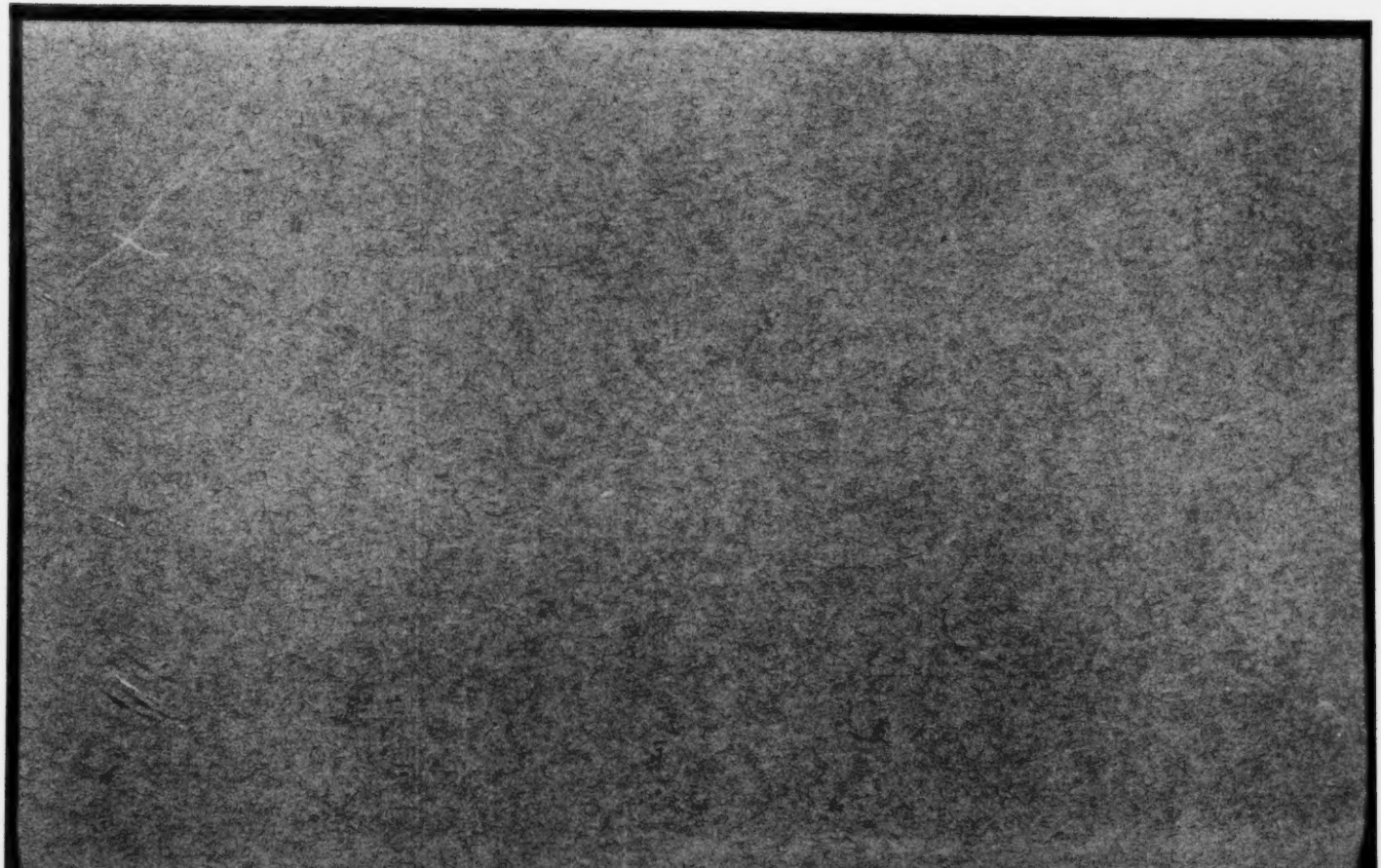
In view of the conflict of authority, and the importance of the questions involved, both to state governments and the federal government, and the taxpayers of the nation, we urge this Court to take over this case by a writ of certiorari and settle the proper rules to govern the matters we have discussed.

We submit that, if the writ is granted, the ultimate decision should reverse the judgment of the Ninth Circuit Court of Appeals and uphold the decision of the District Court for the Southern District of California.

Dated at Los Angeles, California, this 18th day of December, 1941.

REUBEN G. HUNT,
Counsel for Petitioner.

ROBERT B. POWELL,
GRAINGER & HUNT,
Of Counsel.



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440708—42——1

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 838

GEORGE T. GOGGIN, AS TRUSTEE IN BANKRUPTCY OF THE ESTATE OF ACME TRAFFIC SIGNAL COMPANY, A CORPORATION, BANKRUPT, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 2–8) is reported in 37 F. Supp. 352. The opinion of the Circuit Court of Appeals (R. 40–44) is reported in 123 F. (2d) 432.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 18, 1941 (R. 45). The petition for a writ of certiorari was filed on Janu-

ary 5, 1942. The jurisdiction of this Court is predicated upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

In the case of a bankrupt corporation should the capital stock tax imposed by Section 1202 of the Internal Revenue Code and due for a period prior to the adjudication in bankruptcy be computed upon the basis of the value of the capital stock as declared by the company, or upon the basis of the actual value of the company's capital stock?

STATUTES INVOLVED

The statutes involved appear in the Appendix, *infra,* pp. 8–11.

STATEMENT

The petitioner is the trustee in bankruptcy of the Acme Traffic Signal Company, a California corporation, which was adjudicated a bankrupt on May 13, 1940 (R. 9). The petitioner refused to sign a capital stock tax return prepared by the Collector of Internal Revenue for the company for the year ending June 30, 1940, whereupon the Collector made the return pursuant to Section 3612 of the Internal Revenue Code (R. 10). In this return the Collector computed the adjusted declared value for the taxable year by taking the adjusted declared value reported by the company in its 1939 capital stock tax return and deducting therefrom the loss sustained by the taxpayer dur-

ing its previous income tax year (R. 10). The adjusted declared value for the year ending June 30, 1940, was thus computed at $184,966.26, upon which the capital stock tax for the year was assessed (R. 10). It is conceded that the capital stock of the company had an actual fair market value of less than $184,000 on June 30, 1940, and that the trustee in bankruptcy was unable to obtain more than $5,100 upon the sale of all the bankrupt's assets (R. 10). The Collector of Internal Revenue presented a claim in the bankruptcy proceeding for the capital stock tax for the year ending June 30, 1940, as computed by him. The referee allowed the claim (R. 13–14). The District Court vacated the referee's order and held that the capital stock tax should be computed in accordance with the real value of the assets of the company (R. 2–8). The Circuit Court of Appeals for the Ninth Circuit reversed the order of the District Court (R. 45).

ARGUMENT

1. The taxpayer's petition is bottomed upon an erroneous conception of the nature of the capital stock tax imposed by Section 1202 of the Internal Revenue Code (Appendix, *infra,* p. 8). Its premise is that the tax is one levied upon the actual value of the taxpayer's capital stock. All of the questions raised with respect to the powers of bankruptcy courts are based upon this erroneous premise. We submit that when the true nature of the capital stock tax is perceived, the instant

case presents no questions whatever with respect to the powers of bankruptcy courts under Sections 62 (a) and 64 (a)–4 of the Bankruptcy Act (Appendix, *infra,* pp. 10–11).

This Court has several times pointed out the nature of the tax here involved. *Haggar Co.* v. *Helvering,* 308 U. S. 389; *Helvering* v. *Lerner Stores Corp.* (*Md.*), No. 248, decided December 22, 1941; *Scaife Co.* v. *Helvering,* No. 57, decided December 22, 1941. The capital stock tax is integrated with a complementary excess profits tax. The scheme of these taxes is to allow the taxpayer to place any value it chooses upon its capital stock. The tax upon the capital stock and the correlative tax upon excess profits are computed upon that basis. The figure so declared as the value of the capital stock by the taxpayer cannot be amended and is the basic figure for the determination of the value of the capital stock for subsequent years.

The purpose of this statutory scheme, which began with Section 215 of the National Industrial Recovery Act, c. 90, 48 Stat. 195, was to avoid controversy over the actual value of the capital stock. Earlier Revenue Acts had imposed a tax on the capital stock of the corporation measured by "the fair average value of its capital stock." Revenue Act of 1918, c. 18, 40 Stat. 1057, Sec. 1000. The tax was repealed in 1926 because of the administrative difficulty involved in measuring the actual value of capital stock. See S. Rep. No. 52, 69th

Cong., 1st Sess., pp. 11–12 (1939–1 Cum. Bull. (Part 2) 332, 341); 1 Bonbright, Valuation of Property, pp. 577–595. The present form of the tax was adopted expressly "In order to avoid controversy as to the value of the capital stock * * *." S. Rep. No. 114, 73d Cong., 1st Sess., p. 6 (1939–1 Cum. Bull. (Part 2) 881, 882). See also S. Rep. No. 558, 73d Cong., 2d Sess., p. 5 (1939–1 Cum. Bull. (Part 2) 586). It is obvious that under the express statutory plan a declaration of value is never true or untrue, never erroneous or inaccurate, even though mistakenly declared. See the *Scaife* and *Lerner* cases, *supra*. It is therefore impossible for it to be, as the petitioner here contends, "excessive." So far as *Kentucky Fire Brick Co.* v. *Glenn,* 34 F. Supp. 35 (W. D. Ky.), contains language to the contrary it is inconsistent with the foregoing decisions of this Court.

The statute provides that every third year after the year ending June 30, 1938, shall constitute a new "declaration year." In such declaration years a corporation may place a new value upon its capital stock; that value will be conclusive for the ensuing three-year period. Subsection (c) of Section 1202 of the Internal Revenue Code provides that the capital stock tax year beginning with or within an income-tax taxable year within which bankruptcy is terminated shall be a declaration year. In view of this specific treatment of cor-

porations in bankruptcy there is manifestly no basis for any suggestion that the year in which a corporation is adjudicated a bankrupt should be a declaration year. Therefore unless the value placed upon its capital stock by the bankrupt in its last preceding declaration year be taken as the basis for computation of the tax for the year here involved, there is no figure which can be used.

2. No questions as to the power of bankruptcy courts to determine the legality and amount of claimed taxes are presented in this case. So far as Section 64 (a) (4) is concerned, we have conceded throughout this litigation that a bankruptcy court unquestionably has power under that section to determine the amount of taxes due. But such a determination must be made upon the basis of the facts in the case. The most important fact in the determination of the proper amount of taxes due in this case is the fact of the prior declaration of value. Manifestly Section 64 (a) (2) does not give to bankruptcy courts the power to devise a new tax in place of the one enacted by Congress. The District Court's holding that the capital stock tax here should be computed in accordance with the actual value of the company's capital stock amounted to such a substitution of one tax for another. The court below properly reversed that holding.

Section 62 (a) of the Bankruptcy Act is not even remotely involved here. The capital stock tax is imposed upon the doing of business for any

part of the taxable year. The adjudication in bankruptcy did not come until near the end of the taxable year here involved. Since the company had done business for part of the taxable year prior to bankruptcy, it thereupon became liable for the tax. That liability was properly the basis for a claim by the Government in the bankruptcy proceeding. The tax was not claimed because of any operation of the business by the trustee. It was not an expense in administering the bankrupt estate. The same considerations demonstrate that this case presents no question with respect to whether or not the trustee in bankruptcy is a new taxable entity.

CONCLUSION

The decision below is correct. No questions are presented with respect to the capital stock tax which are not governed by the decisions of this Court. No questions with respect to the Bankruptcy Act are presented at all. The petition should be denied.

Respectfully submitted.

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JANUARY 1942.

APPENDIX

Internal Revenue Code:

SEC. 1202. ADJUSTED DECLARED VALUE.

(a) *Declaration Year.*—

(1) The adjusted declared value shall be determined with respect to three-year periods beginning with the year ending June 30, 1938, and each third year thereafter. The first year of each such three-year period, or, in case of a corporation not subject to the tax imposed for such year, the first year of such three-year period for which the corporation is subject to such tax, shall constitute a "declaration year."

(2) For the declaration year of the first three-year period the adjusted declared value shall be the value as declared by the corporation in its return under section 601 of the Revenue Act of 1938, 52 Stat. 565, for the year ended June 30, 1938, or in the case of a corporation not subject to the tax imposed for such year, the value as declared in its return filed under this chapter for the first year with respect to which it is subject to the tax. For each subsequent three-year period, the adjusted declared value for a declaration year shall be the value as declared by the corporation in its return for such declaration year. The value declared by a corporation in its return for a declaration year (which declaration of value cannot be amended) shall be as of the close of its last income-tax taxable year ending with or prior to the close of such declaration year

(or as of the date of organization in the case of a corporation having no income-tax-taxable year ending with or prior to the close of such declaration year).

(b) *Subsequent Years.*—

(1) *Domestic corporations.* — For each year of any three-year period subsequent to the declaration year, the adjusted declared value in the case of a domestic corporation shall be the value declared in the return for the declaration year plus—

(A) the cash, and the fair market value of property, paid in for stock or shares,

(B) paid-in surplus and contributions to capital,

(C) its net income,

(D) its income wholly exempt from Federal income tax, and

(E) the amount, if any, by which the deduction for depletion exceeds the amount which would be allowable if computed without regard to discovery value or to percentage depletion, under section 114 (b) (2), (3), or (4) of chapter 1 or a corresponding section of a later Revenue Act;

and minus—

(i) the cash, and the fair market value of property, distributed to shareholders,

(ii) the amount disallowed as a deduction by section 24 (a) (5) of chapter 1 or a corresponding provision of a later Revenue Act, and

(iii) the excess of the deductions allowable for income tax purposes over its gross income.

The adjustments provided in this paragraph shall be made for each income-tax taxable year included in the three-year period from the date as of which the value was declared in the return for the declaration

year to the close of the last income-tax taxable year ending with or prior to the close of the year for which the tax is imposed by this section. The amount of such adjustment for each such year shall be computed (on the basis of a separate return) according to the income tax law applicable to such year.

(2) *Foreign corporations.*—For each year of any three-year period subsequent to the declaration year, the adjusted declared value in the case of a foreign corporation shall be the value declared in the return for the declaration year adjusted (for the same income-tax taxable years as in the case of a domestic corporation), in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, to reflect increases or decreases in the capital employed in the transaction of its business in the United States.

(c) *Corporations in Bankruptcy or Receivership.*—The capital-stock tax year beginning with or within an income-tax taxable year within which bankruptcy or receivership, due to insolvency, of a domestic corporation, is terminated shall constitute a declaration year. In such case the adjusted declared value for any subsequent year of the three-year period shall be determined on the basis of the value declared in the return for such declaration year.

* * * * *

(U. S. C., Title 26, Sec. 1202.)

Bankruptcy Act of July 1, 1898, c. 541, 30 Stat. 544, as amended by the Act of June 22, 1938, c. 575, 52 Stat. 840:

SEC. 62. EXPENSES OF ADMINISTERING ESTATES: UNAUTHORIZED SHARING OF FEES: WITHHOLDING ALLOWANCES.—a. The actual

and necessary costs and expenses incurred by officers in the administration of estates, shall, except where other provisions are made for their payment, be reported in detail, under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred.

* * * * *

(U. S. C., Title 11, Sec. 102.)

SEC. 64. DEBTS WHICH HAVE PRIORITY.—a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be * * * (4) taxes legally due and owing by the bankrupt to the United States or any State or subdivision thereof: *Provided,* That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further,* That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; * * *

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(U. S. C., Title 11, Sec. 104.)

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